No. 22143

United States Court of Appeals

For the Ninth Circuit

PENNALUNA & COMPANY, INC.
BENJAMIN A. HARRISON, and
HARRY F. MAGNUSON, *Petitioners,*

v.

SECURITIES EXCHANGE COMISSION,
Respondent.

PETITION FOR REVIEW OF ORDER OF SECURITIES EXCHANGE COMMISSION

BRIEF OF PETITIONERS PENNALUNA & COMPANY, INC. BENJAMIN A. HARRISON, and HARRY F. MAGNUSON

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BRIEF OF PETITIONERS PENNALUNA & COMPANY, INC. BENJAMIN A. HARRISON, and HARRY F. MAGNUSON

I.

JURISDICTIONAL STATEMENT

This case is before this court on a joint petition filed on behalf of Pennaluna & Company, Inc., Benjamin A. Harrison, and Harry F. Magnuson for review of an order of the Securities & Exchange Commission dated April 27, 1967, revoking the registration of petitioner Pennaluna & Company, Inc. barring petitioner Benjamin A. Harrison and petitioner Harry F.

Magnuson from association with any broker or dealer, and expelling petitioner Benjamin A. Harrison from membership in the Spokane Stock Exchange, and on the petition of the same parties for review of the order of the Securities Exchange Commission (hereinafter referred to as respondent) dated July 6, 1967, denying petitioners' joint petition for reconsideration. The order of the respondent dated April 27, 1967, appears at page 4608-4622 of the Record herein and the order of the respondent dated July 6, 1967, is found on pages 4661, 4662 of the Record herein. On September 1, 1967 an additional petition and motion for further rehearing, reconsideration and review was filed by petitioners; it was rejected by the respondent on September 12, 1967. (Supp. R. 4690-4699).

This action was commenced by an order for private proceedings issued by the respondent on October 1, 1964. (R. 65-71).

This court has jurisdiction to entertain this petition under the provisions of Section 25 of the Securities Exchange Act. (15 USCA 78y). Section 25 provides in part as follows:

> SECTION 25. (a) Any person aggrieved by an order issued by the Commission in a proceeding under this title to which such person is a party may obtain a review of such order in the Court of Appeals of the United States, within any circuit wherein such person resides or has his principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the entry of

such order, a written petition praying that the order of the Commission be modified or set aside in whole or in part.

Petitioner Benjamin A. Harrison is a resident of the City of Spokane, State of Washington. Petitioner Harry F. Magnuson is a resident of the City of Wallace, State of Idaho. Petitioner Pennaluna & Company, Inc. is a registered broker-dealer and has its principal place of business in the City of Spokane, State of Washington. The residence and principal place of business of each of the petitioners is found within this circuit. The petition for review was presented timely within 60 days after the entry of the final order of the respondent dated July 6, 1967.

The statutes involved in this action include Section 5 and Section 17(a) of the Securities Act of 1933 (15 U.S.C.A. 77e, 77q) and Sections 10(b), 15(b), 15 (c)(1), 19(a)(3) of the Securities Exchange Act of 1934 (15 U.S.C.A. 78j, 78o, 78s) and the rules of the respondent promulgated thereunder.

The order for private proceedings alleges violations of the above statutes in offering to sell, selling and delivering after sale the common stock of Silver Buckle Mining Company, an Idaho corporation, during the period from about May 8, 1962 to about June 10, 1963, and the common stock of West Coast Engineering, Inc., a Washington corporation, into which Silver Buckle Mining Company was merged on June 10, 1963, during the period from about that date to about April 30, 1964. (R. 68-70). It is further

alleged that the petitioners extended credit to certain customers in contravention of Section 4 (c) (2) of Regulation T promulgated by the Board of Governors of the Federal Reserve System and failed to make and keep current certain records required by Section 10(a) and Section 17(a) of the Securities Exchange Act (15 U.S.C.A. 78j, 78q) and rules of the respondent promulgated thereunder. (R. 69-71).

The record in this matter includes depositions of the petitioners and other witnesses together with exhibits submitted on behalf of the petitioners, witnesses and the respondent at each deposition. The record further includes a stipulation of facts entered into between the petitioners and members of the Division of Trading and Markets of the respondent on June 4, 1965, which stipulation was entered into for the purpose of providing the respondent with a basis for determining the evidentiary questions in this proceeding and for the further purpose of eliminating the need for a hearing to take evidence on the question set forth in Section 3 of the order for private proceedings. (R. 65-71). It was further understood in said stipulation that it included all the various exhibits, transcripts of testimony and related exhibits. (R. 129). The following facts were admitted by petitioners (R. 130-131): (1) the jurisdictional basis for applying Section 5 and Section 17(a) of the Securities Act, and Section 10(b) and 15(c)(1) of the Securities Exchange Act and the rules promulgated by respondent thereunder; (2) that petitioners did transact a business in securities through

the medium of members of national securities exchanges, (3) that the petitioner Pennaluna & Company, Inc., (and its predecessor Pennaluna and Company) is a registered broker-dealer in securities pursuant to Section 15(b) of the Securities Exchange Act (15 U.S.C.A. 78o).

II.

STATEMENT OF THE CASE

The Pennaluna & Company was registered with the respondent as a broker-dealer partnership pursuant to Section 15(b) of the Securities Exchange Act of 1934 (15 U.S.C.A. 78o) on September 1, 1954 and continued in that capacity until January 16, 1964. (R. 136). From December 26, 1961 forward the partnership consisted of the petitioner Benjamin A. Harrison and the petitioner Harry F. Magnuson with Harrison owning a 62½ percent interest and Magnuson owning the remaining 37½ percent. (R. 136). On September 16, 1963, the petitioner Pennaluna & Company, Inc. (hereinafter referred to as "Pennaluna") was incorporated in the State of Idaho and, since that time, the petitioner Benjamin A. Harrison (hereinafter referred to as "Harrison") has been the president of Pennaluna. (R. 137). The petitioner Harry F. Magnuson (hereinafter referred to as "Magnuson") continued as its Secretary-Treasurer until August, 1965. (R. 137; R. 22). As shown by the amendment to the broker-dealer application received by the respondent on August 27, 1965, Harrison owned all the

common stock of Pennaluna at that date. (R. 22). The registration of Pennaluna in its corporate form became effective on November 29, 1963. (R. 40).

During the time that Magnuson was an officer and director of Pennaluna, he supervised the Wallace and Kellogg offices, excluding the trading activities, and was responsible for the record-keeping activities of Pennaluna conducted at the Wallace office. (R. 152). Harrison was in charge of all trading activities of Pennaluna and the operation of the Spokane office. (R. 152). Pennaluna primarily deals in securities issued by mining companies with mineral properties in Idaho, Montana, Utah, Washington and British Columbia, and trades such securities for the most part on a wholesale basis with other broker-dealers and only to a lesser degree with retail customers. (R. 140).

Silver Buckle Mining Company

Silver Buckle Mining Company (hereinafter referred to as "Silver Buckle") was incorporated under the laws of the State of Idaho in 1947 with a capitalization of 10 million shares of non-assessable stock, having a par value of 10 cents. (R. 2185). Dr. Frank E. Scott, a dentist residing in Wallace, Idaho, has been involved in numerous mining ventures and was instrumental in the incorporation of Silver Buckle. (R. 157). On January 8, 1954, 378,333 shares of Silver Buckle were issued to Oil, Inc., (hereinafter referred to as Oil, Inc.) a company of which Mr. W. H. H. Cranmer was president at that time. (R. 4316-4319

and R. 2194). Mr. Cranmer was also president of New Park Mining Company (hereinafter referred to as "New Park") and East Utah Mining Company (hereinafter referred to as "East Utah"), and Mr. Clark L. Wilson was Vice-President and Manager of operations of New Park and Superintendent of East Utah; as shown on an offering circular, New Park and East Utah owned 378,334 and 378,333 shares respectively of the common stock of Silver Buckle as of April 3, 1954. (R. 2194). These purchases were all made under stock options previously granted to Cranmer. (R. 2198). On that date, Dr. Frank Scott and Mr. Jack Gay jointly held 390,000 shares of Silver Buckle; Dr. Scott individually owned 187,578 shares and Mr. Gay owned an additional 390,000 shares. (R. 2194). During 1953 and 1954 Silver Buckle entered into joint operating agreements with Vindicator Silver Lead Mining Company and entered into a development agreement with the Defense Minerals Exploration Administration. Silver Buckle also had acquired an assignment of certain mineral leases in Utah, adjacent to a recent uranium discovery. (R. 2198). These mineral leases were acquired from Oil, Inc., New Park and East Utah in exchange for 666,666 shares of Silver Buckle stock distributed equally among the three companies.

As stated in the report to shareholders dated October 25, 1956, Silver Buckle's mining claims adjoin the Vulcan Mine operated by American Smelting & Refining Company and Day Mines, Inc. (R. 2233).

Silver Buckle also was continuing its interest in t
Vindicator Mine, located near Mullen, Idaho, whi
adjoined the Lucky Friday Mine, now owned and ope
ated by Hecla Mining Company. (R. 2233). Silv
Buckle was developing its interest in the big Indi
Wash area of the Southern Utah Uranium field und
an operating agreement with National Uranium Co
pany. (R. 2233). Silver Buckle had acquired 160,0
shares of Lucky Mac Uranium Corporation (R. 223
These assets, together with the other assets of Silv
Buckle, had greatly increased and diversified. (
2233A).

The annual report for Silver Buckle for the peri
ending July 31, 1960 indicated that the uranium ope
ations of Silver Buckle had been quite profitable du
ing the ensuing four years. Uranium leases acquir
on the Spokane Indian reservation had been sold
Dawn Mining Company and were being operated
that company pursuant to a contract with the Atom
Energy Commission. (R. 2237). After reimburseme
for its expenses and advancements, Silver Buck
expected to realize approximately $112,000.00 from t
sale of these leases. (R. 2237). The financial sta
ment attached to the annual report indicated th
Silver Buckle now held liquid assets in the form
cash and marketable securities in excess of $1 milli
dollars. (R. 2238, 2239; R. 164).

7,459,243 shares were issued and outstanding in Ju
1961, (R. 2185), with approximately 3,500 shareholde
(R. 1945). New Park and East Utah jointly held abo

1,417,000 shares of Silver Buckle; Oil, Inc. still held 600,555 shares. Dr. Scott, Jack Gay and Nolan Brown held approximately 1,025,000 shares as a group. (R. 1946). Dr. Scott was president and director; Clark Wilson was Vice President, General Manager and director; Alden Hull was Secretary-Treasurer and director; W. H. H. Cranmer and Nolan Brown were also directors. (R. 2185; R. 163). An additional 2,000,000 shares were committed for issuance as a result of the West Coast agreement described below; consequently, as of November 11, 1961, 9,459,243 shares were considered issued and outstanding.

Magnuson and Harrison have never been officers or directors of Silver Buckle. Sometime during the above period, Magnuson received 542 shares of Silver Buckle; these were the only shares held beneficially by him until May 8, 1962 (R. 158). Magnuson was a director of Vindicator but it is stipulated that he took no part in the negotiations for the Silver Buckle-Vindicator development contract or the purchase by Silver Buckle of Vindicator stock. (R. 161).

West Coast Engineering, Inc.

West Coast Engineering, Inc., (hereinafter referred to as "West Coast") was incorporated by Mr. Bryan J. Dickinson on October 6, 1960. (R. 165; R. 2245). As shown by an offering circular filed with the Securities Exchange Commission on September 1, 1961, the original objective of the company had been the sale of earth moving and mining equipment in the states of

Silver Buckle also was continuing its interest in the Vindicator Mine, located near Mullen, Idaho, which adjoined the Lucky Friday Mine, now owned and operated by Hecla Mining Company. (R. 2233). Silver Buckle was developing its interest in the big Indian Wash area of the Southern Utah Uranium field under an operating agreement with National Uranium Company. (R. 2233). Silver Buckle had acquired 160,000 shares of Lucky Mac Uranium Corporation (R. 2233). These assets, together with the other assets of Silver Buckle, had greatly increased and diversified. (R. 2233A).

The annual report for Silver Buckle for the period ending July 31, 1960 indicated that the uranium operations of Silver Buckle had been quite profitable during the ensuing four years. Uranium leases acquired on the Spokane Indian reservation had been sold to Dawn Mining Company and were being operated by that company pursuant to a contract with the Atomic Energy Commission. (R. 2237). After reimbursement for its expenses and advancements, Silver Buckle expected to realize approximately $112,000.00 from the sale of these leases. (R. 2237). The financial statement attached to the annual report indicated that Silver Buckle now held liquid assets in the form of cash and marketable securities in excess of $1 million dollars. (R. 2238, 2239; R. 164).

7,459,243 shares were issued and outstanding in June 1961, (R. 2185), with approximately 3,500 shareholders (R. 1945). New Park and East Utah jointly held about

1,417,000 shares of Silver Buckle; Oil, Inc. still held 600,555 shares. Dr. Scott, Jack Gay and Nolan Brown held approximately 1,025,000 shares as a group. (R. 1946). Dr. Scott was president and director; Clark Wilson was Vice President, General Manager and director; Alden Hull was Secretary-Treasurer and director; W. H. H. Cranmer and Nolan Brown were also directors. (R. 2185; R. 163). An additional 2,000,000 shares were committed for issuance as a result of the West Coast agreement described below; consequently, as of November 11, 1961, 9,459,243 shares were considered issued and outstanding.

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Washington and Alaska; (R. 2241) however, the company began to emphasize the manufacture and lease of indoor, automatic archery lanes. (R. 2242). This new enterprise was publicized by newspaper and magazine articles, as shown by clippings in the West Coast scrapbooks. (Scrapbooks I and II). One installation consisting of 16 archery lanes had been completed on August 25, 1961, and had been leased for a period of seven years to a partnership composed of two directors of West Coast. (R. 165; R. 2242) (Scrapbook I). The administration office, warehouse and manufacturing facilities of the company were maintained at 2427 Sixth Avenue South, Seattle, Washington. (R. 2242). The offering circular further disclosed that the company had not obtained patents as yet for the integral portion of its automatic archery lanes and that it had no assurance that the company could successfully develop or market the patented product. (R. 2242). The directors of the corporation were Bryan Dickinson, Willard Dziuk, Ethel Crial, Clark Conrad, William Johnson and William Delbridge. (R. 2243).

Only a few shares were sold under this offering and, by mid-October 1961, West Coast had a serious need for further developmental funds. (R. 165). In an effort to obtain further financing, Dickinson contacted a number of persons and mining companies in Wallace, Idaho, who might be interested in providing venture capital. (R. 166). Harry Magnuson was among those persons contacted. (R. 166). Dickinson called at Magnuson's office, but Magnuson was too busy to discuss West Coast's financing problems with him. (R. 1132).

Dickinson eventually contacted Scott and Gay. As a result of the subsequent discussions between them and an investigation by Gay into the prospects for automated archery, an agreement was entered into between Silver Buckle and West Coast on November 10, 1961. (R. 2268-2275). Under the terms of that agreement, Silver Buckle advanced West Coast $60,000.00, evidenced by a promissory note payable upon 90 days demand, with interest at the rate of 6 percent per annum beginning 90 days after date on a declining balance. The note was convertible to 30,000 shares of common stock of West Coast at the option of Silver Buckle and, in the event that Silver Buckle elected to so convert, they would then have the further option to acquire 150,000 shares of West Coast at the price of $2.00 per share. (R. 2269, 2270). Silver Buckle also acquired the independent right to acquire 50,000 shares of West Coast and, in the event that such acquisition was made, Silver Buckle had the right to acquire an additional 250,000 shares of West Coast at $2.00 per share on the same time schedule as established for the other option agreements. (R. 2270). By exercising its conversion rights, Silver Buckle would become entitled to one or more representatives on the board of directors of West Coast and have the eventual right to acquire a majority representation on the board. (R. 2271). Silver Buckle had the further option to exchange 1,999,998 shares of its capital stock for 285,714 shares of capital stock of West Coast. (R. 2273).

The agreement was executed by Dr. F. E. Scott, president of Silver Buckle, and Bryan Dickinson, president of West Coast. (R. 2274).

As a result of this agreement, Silver Buckle had the ability to acquire 92 percent of the stock of West Coast. As shown in a note attached to the financial statement for West Coast for the year ending December 31, 1961, and the two months ending February 28, 1962, Silver Buckle executed certain of the above options on February 6, 1962. Silver Buckle owned 54.5 percent of West Coast's stock as of that date. (R. 2266). Silver Buckle eventually purchased 88.41 percent of West Coast's outstanding stock.

In conjunction with this agreement, Gay became a participant in West Coast's business affairs and had the ability to co-sign West Coast's checks. (R. 168). Following the directors meeting held February 6, 1962, Scott, Hull and Brown were elected to West Coast's 5-man board; the other two directors were Dickinson and Dziuk. Dickinson continued as president of West Coast; Gay became Executive Vice President and Dr. Scott became Secretary. Nolan Brown also became Treasurer. Pursuant to resolution, the directors of Silver Buckle also agreed to guarantee all of West Coast's present and future contractual indebtedness. (R. 171).

The Silver Buckle stockholders letter, dated February 21, 1962, stated that Silver Buckle had purchased

a controlling interest in West Coast for an investment of $160,000.00. (R. 172; R. 2309-2311).

It is stipulated that neither Magnuson nor Harrison knew of this agreement between Silver Buckle and West Coast until the stockholders letter was received. (R. 159 and R. 167). Magnuson testified that he had no interest in Silver Buckle and consequently was not involved in any of the discussions taking place between October, 1961, and February, 1962. (R. 1134). Except for the fact that Magnuson and Scott were both directors of Vindicator and Ruby Silver Mines, Inc., Magnuson had not had any business arrangements with either Scott or Gay. (R. 1128).

The Oil, Inc. Transaction

On March 2, 1962, W. H. H. Cranmer was removed as president and general manager of New Park (R. 4158-4161); he was also removed as president of East Utah, and his son Robert L. Cranmer, was removed as executive vice president of East Utah on May 3, 1962. (R. 4151). These actions were taken as a result of the acquisition of control of New Park and East Utah by Mr. Charles Steen during late 1961 and early 1962. (R. 174, 175 and 176). Mr. Robert L. Cranmer previously had been named president of Oil, Inc. by his father and he continued in that position. The new management of East Utah and New Park was unable to exert any control over his activities or the activities of his company. (R. 4168; R. 4158-4161; R. 4163-4167).

Robert Cranmer was able initially to retain the Cranmer family control of Oil, Inc. but he needed money to withstand the Steen attack. (R. 1982). The Silver Buckle shares were an obvious source of funds. The Minutes of a special meeting of the Board of Directors of Oil, Inc., held May 8, 1962 revealed that another purpose of the subsequent sale of Silver Buckle shares was to meet outstanding obligations of Oil, Inc. (R. 2371, 2372). Cranmer contacted Dr. Scott concerning the possibility of Silver Buckle purchasing the 600,555 shares of Silver Buckle stock owned by Oil, Inc. (R. 176; R. 1982). Dr. Scott and Cranmer worked out an arrangement for the sale of these shares by Oil, Inc. for 10c per share, or $60,055.00. (R. 176). In a letter to the Seattle Regional Office of the respondent dated February 1, 1965, in response to a subpoena duces tecum, the treasurer of Oil, Inc. stated that the sale negotiations were conducted by telephone between the officers of Oil, Inc. and the officers of Silver Buckle. (R. 176; R. 2367). Having negotiated the sale, Dr. Scott approached Magnuson to see if he was interested in participating in the purchase. (R. 1983; R. 1138). Magnuson testified that he was totally unfamiliar with the details of the West Coast agreement and became interested in Silver Buckle only because of its potential as a silver company. (R. 1138). He further testified that he did not know that Silver Buckle's liquid assets had been committed to West Coast. (R. 1140). He had not seen the financial statement of West Coast for the period ending February 28, 1962. (R. 1145). Magnuson stated to Scott that he was

nterested in purchasing a portion of these shares for his own account and that he and Scott should contact others who might also be interested. Among the persons contacted was Harrison on behalf of Pennaluna. (R. 178; R. 1148).

The Silver Buckle shares were deposited by Oil, Inc. n escrow with the Wallace Branch of the Idaho First National Bank. (R. 176; R. 2373). Pursuant to the corporate resolution of Oil, Inc., Magnuson's personal account became the medium into which payments were deposited by the various purchasers. (R. 2371). The total amount of deposits having been made, a cashier's check for $59,995.50 (the purchase price less collection charge) was remitted to Oil, Inc. on May 18, 1962. (R. 2382; R. 2389). The two certificates were broken down among the various persons who had deposited the money into the escrow account by the transfer agent for Silver Buckle upon written instructions from Magnuson. (R. 2366). Certificates in the name of Pennaluna were issued for 461,555 shares; it is stipulated that Pennaluna had a beneficial interest in only 90,555 shares. (R. 2366; R. 177). Pennaluna had issued a check for $9,055.50 directly to the Idaho First National Bank, which required H. F. Magnuson's endorsement before being deposited in the escrow account. (R. 2378, 2379). Magnuson, and accounts for his children of which he was custodian, actually paid for 172,000 shares. (R. 178). Scott purchased 14,000 shares. (R. 178). The remaining 324,000 shares were divided among persons whom both Magnuson

and Scott had contacted (R. 179, 180) (See list of purchasers, Appendix page 2).

The shares purchased by Pennaluna were placed in its trading account and, on a first-in first-out basis, were sold in the normal course of trading by July 14, 1962, at prices ranging from 13 cents to 20 cents per share. (R. 182; R. 2395, 2396).

The New Park-East Utah Transaction

A geologist had examined Silver Buckle's silver properties at the request of Charles Steen, and, during July or August, 1962, Steen informed Scott that Steen was going to have Scott removed as president of Silver Buckle. (R. 196). Meetings and conversations were held between Steen and Scott, but they were unable to resolve their differences. (R. 2010). New Park and East Utah prepared a complaint against Silver Buckle to be filed in the District Court of Salt Lake County, State of Utah; the complaint is dated August 17, 1962, and demanded that the plaintiffs be permitted to inspect the corporate books of Silver Buckle. (R. 4192, 4193). Steen also decided to commence selling blocks of Silver Buckle stock owned by New Park and East Utah through the Cromer Brokerage Company of Salt Lake City, Utah. (R. 196). Silver Buckle refused to honor the transfer request made on August 22, 1962 for 222,222 shares. At Silver Buckle's request, the transfer was effected only upon receiving a legal opinion from the attorneys for New Park and Cromer Brokerage Company that New

Park did not exercise a controlling influence upon Silver Buckle because of the dispute between the companies. (R. 196; R. 2183).

During the summer months of 1962, Ruby Silver Mines, Inc. was in the process of preparing a Regulation A public offering of its shares. Magnuson was a director of this company for the purpose of representing Pennaluna, an underwriter of the proposed issue. (R. 189). About the middle of September, 1962, Magnuson first became aware that New Park and East Utah, who were also principal stockholders of Ruby Silver, might take legal steps to oppose the public offering of Ruby Silver shares. (R. 197). Magnuson testified that he had been a rather inactive participant in the affairs of Ruby Silver, had not attended a meeting and had not been involved in its organization. (R.1181). In order to protect Pennaluna's underwriting commission and Ruby Silver's public offering, Magnuson contacted David Clegg, the attorney for New Park and East Utah at that time, and, at Clegg's request, arranged a meeting of all parties in Spokane to discusse Dr. Scott's differences with New Park and East Utah. (R. 197; R. 1185; R. 1197). The general framework of the discussion had already been established by Scott and Steen. (R. 1195).

As a result of the meeting held in Spokane, Washington, September 29, 1962, between Magnuson, Clegg, Scott and Alden Hull, an attorney for Silver Buckle, a plan of settlement was evolved which called for two

separate contracts. The first contract was between Silver Buckle, New Park and East Utah, and the second contract again used Magnuson's name as purchaser, and New Park and East Utah, as sellers. (R. 198; R. 1394-1407). Silver Buckle agreed to repurchase 367,111 of its shares and the companies agreed to cancel various claims and demands among them, including the Ruby Silver dispute. The remaining 800,000 shares were sold under the second contract for 20c per share, (slightly less than the average offer quote on the Spokane Exchange on September 28, 1962, (R. 2441), or a total of $160,000.00. Magnuson was concerned only with the latter contract. (R. 1206). At Magnuson's request, the handwritten form of this contract stated that New Park and East Utah warranted that the stock was not subject to any SEC restrictions. (R. 1214; R. 2592). Clegg, an attorney, also told Magnuson that the stock could be traded. (R. 1216). Hull and Clegg drew the agreement. (R. 1215).

Magnuson testified that he did not feel he could influence the management of Silver Buckle and that he was not the controlling person at this time. (R. 1218). He received a legal opinion from Piatt Hull, a Wallace attorney, on October 5, 1962; that opinion stated that Magnuson was not a person in direct or indirect control of Silver Buckle based upon his recent acquisitions of Silver Buckle shares, shares owned by his children and shares purchased by Pennaluna. (R. 1229; Appendix page 5). Dr. Scott further testified that the group controlling Silver Buckle in-

cluded Gay, the Browns, the West Coast directors and himself. (R. 2050). This group continued to control Silver Buckle until the merger of June, 1963. (R. 2051).

Dr. Scott previously had agreed to be responsible for the purchase of 300,000 shares and Pennaluna, through Harrison, had agreed to purchase 200,000 shares (R. 199, 200; R. 1427). The Scott commitment was confirmed by Magnuson by letter dated October 1, 1962, which set forth the due date and amount of Scott's payments. (R. 2608).

The Spokane National Bank, Spokane, Washington, was designated as the escrow agent; certificates for 700,000 shares were transmitted by New Park directly to the bank, together with escrow instructions. (R. 2609). Pennaluna purchased 100,000 shares with a check for $20,000 to New Park and East Utah, signed by Magnuson with Harrison's authorization, at the completion of negotiations on September 29, 1962. (R. 199; R. 4194). A purchase of 100,000 shares on September 29, 1962, was reported properly to the respondent in its December questionnaire. (R. 253; R. 4320).

Various persons contacted by Dr. Scott eventually purchased a total of 220,000 shares. (R. 201) Magnuson actually purchased a total of 370,000 shares for himself and his custodian accounts of which 300,000 shares are still held by him as part of the shares now owned in the reorganized company. (R. 1212). Pennaluna purchased its remaining 100,000 shares by checks for

$10,000 each, dated November 26, 1962 and January 14, 1963, and also paid its share of the escrow fee. (R. 278; R. 3029, 3030, 3031) (See list of purchasers, Appendix page 4).

After receipt of the certificate for the 100,000 shares during the latter part of October, Harrison entered the purchase in the trading ledger of Pennaluna in blocks of 20,000 shares each @ 21c per share, on November 1, 1962, November 2, 1962, November 30, 1962, December 3, 1962 and December 5, 1962; these shares were sold in the normal course of trading activity by Harrison during this period. (R. 2402, 2410, 2411). New Park was shown as the seller.

Representatives of the Seattle Regional Office conferred with Magnuson on January 10, 1963 and advised him that they had some questions concerning the control aspects of the purchase of Silver Buckle stock from New Park and East Utah. (R. 278, 279; R. 3014, R. 4613). Harrison knew the substance of this conversation. (R. 279) The second block of 100,000 shares was not entered in the trading ledger but was charged to the drawing accounts of Harrison and Magnuson on January 12, 1963, partially as a result of this discussion. The certificates, after release from escrow, were placed in a special envelope. (R. 279).

On about March 5, 1963, Silver Buckle sent a letter to Harrison and other brokers concerning the SEC investigation of Silver Buckle stock prices and sales of Silver Buckle stock acquired from New Park and

East Utah in September, 1962. (R. 302; Appendix page 86). That letter stated that the sellers of the stock had relied upon the advice of their counsel that registration was not required and that neither the Securities Act of 1933 nor the Securities Exchange Act of 1934 imposed any restrictions upon trading in the presently outstanding shares of the company except for certain restrictions with respect to unnamed controlling persons. Commencing May 2, 1963, and continuing through June 18, 1963, Pennaluna purchased the 100,000 shares charged to the drawing account of Harrison and Magnuson through a nominee, Jerry T.O'Brien, who received $500.00 for his participation in these transactions; both partners received their proportionate interest in the proceeds of sale. (R. 319, 320). O'Brien was shown as the seller on Pennaluna's trading ledger. (R. 2434-2437).

Magnuson testified that the sale was made through O'Brien in order to segregate the transaction from the normal trading activities of Pennaluna, to complete the transaction for purposes of meeting capital gain requirements, and to hide the transaction from the other employees of Pennaluna. (R. 1360; R. 1366). It was the policy of Pennaluna to discourage trading activities by its employees. Magnuson further testified that he thought the discussion on January 10, 1963 related to the 300,000 shares that he had purchased from New Park and East Utah and which were still in escrow at the time of the discussion. (R. 1363). Those shares were deposited with the Peoples National Bank

of Washington as collateral for a loan on about January 10, 1963. (R. 279).

Harrison has never held securities for a personal investment of any kind. Magnuson handled all details of this transaction. (R. 871, 872).

West Coast Publicity and Financing Activity

The Burien, Washington archery range opened about September 1, 1961 amidst widespread publicity and newspaper coverage. (See material in Scrapbook I). The Lessor's interest in the lease was sold to Lease Equipment Co. for $86,733.60 on September 17, 1962 with recourse against West Coast for any delinquent rental payments. (R. 203; 2619-2631).

West Coast began an intensive publicity campaign on or about August 15, 1962 to promote the opening of the Golden Arrow Archery Lanes, Denver, Colorado, on September 28, 1962. (R. 203; R. 2611). The Denver archery range attracted nation-wide attention, as did the subsequent openings of the archery lanes at Portland, Oregon (November 9, 1962), Downey, California (December 13, 1962), and Covina, California (December 31, 1962). (R. 204; R. 260). Each opening was followed by a three-week TV, radio and publicity advertising campaign. (See pages 48-64 of Appendix for a sample of the press kit.)

Newspaper articles appeared in the Denver Post, Rocky Mountain News (Denver), Southeast News

(Downey) Downey Herald American, Portland Oregonian, Los Angeles Herald Examiner, Los Angeles Times, Kalamazoo, Michigan Gazette, Detroit Press and many other newspapers throughout the nation. (Scrapbook I, page 41, 42; Scrapbook II, page 5, 6, 25; Scrapbook III and IV). These articles appeared almost daily during the Fall of 1962 and early Spring of 1963.

Magazine articles appeared in the December, 1962 issue of International Management, (McGraw-Hill Publication) page 67 (Scrapbook I), September, 1962 issue of Popular Mechanics (Scrapbook II, page 5), December, 1962 issue of Western Machinery and Steel World (Scrapbook II, page 11) and other business and archery magazines. (Scrapbook III and IV).

Extensive publicity during this period also accompanied the opening of archery ranges by World Wide Indoor Automatic Archery Lanes, a competitor of West Coast, partially an archery range at Boise, Idaho. (Scrapbook II, page 27).

This publicity attracted the interest of numerous brokerage firms and financial houses; in response to inquiries, Gay sent brochures and other general information to representatives of Pacific Northwest Company, Cruttenden, Podesta & Miller, Blythe & Company, J. May & Company, Parks & Co., the research department of Bache & Company and several other firms. (R. 204; R. 1592; R. 1712; R. 2883; R. 4155; R. 4196-4210).

On October 13, 1962, an illustrated article concerning West Coast and the Denver opening appeared in Business Week. (R. 224; Scrapbook II, page 6). Gay testified that the article was the product of Dickinson and the West Coast public relations department and related directly to the Denver opening. (R. 1602). The article inaccurately referred to twenty million dollars worth of business; Gay recognized that the figure was inaccurate and requested West Coast salesmen to use the seven million dollar figure that had previously been approved by him. (R. 224; R. 1604; R. 1675-1677). Reprints of this article were distributed by West Coast to broker-dealer firms inquiring for information and the article was received by Pennaluna without Pennaluna's knowledge of the inaccuracy of the statement. (R. 225). The October 15, 1962 issue of Newsweek described an archery installation and its costs. (Scrapbook II, page 6).

Magnuson was in Seattle on October 3, 1962, and talked with Jack Gay; however, he did not ask for any financial information and testified that he would not have obtained it if he had asked for it. (R. 1254). Gay and he were not friendly at that time. (R. 1255). On October 9, 1962, he sent some tax suggestions to Dr. F. E. Scott; however, his suggestions were not accepted. (R. 218; R. 2739). Magnuson and Harrison attended the opening of the Portland range on November 19, 1962, as did many other brokers. (R. 910; R. 1273). Magnuson offered the assistance of Golconda Mining Corporation if West Coast should need addi-

tional equity capital; this offer was refused flatly by Gay. (R. 1273-1275) (Magnuson is an officer and director of Golconda Mining Corporation, an Idaho corporation (R. 2885)). No financial information was sought or obtained by Harrison. (R. 845). Brokers in Portland were very enthusiastic (R. 845). Magnuson had no knowledge of the financial condition of West Coast, Silver Buckle or the Burien and Denver Archery Lanes at this time; nor did he know about Silver Buckle's unconditional guarantee or its guarantee of the Burien lease. (R. 1275; R. 1331; R. 1862-1866). He saw a Silver Buckle financial statement sometime during the fall of 1962, but it contained no information concerning West Coast. (R. 1314-1316). Scott and Gay also testified that Magnuson did not request financial information during the fall of 1962. (R. 1324; R. 1627; R. 2093).

During the fall of 1962, West Coast was attempting to obtain long-range financing. (R. 1872-1877; R. 4155; R. 4196-4210). Until West Coast could sell its Lessor's interest in the leases, Gay knew there would be a shortage of interim capital. (R. 1625). Richard Snyder, a recreation consultant, made a favorable report to Midwest Oil Company as a result of his study of the Denver opening; Vickers Oil Company also made a survey. (R. 220). Agreements actually were prepared between West Coast and Midwest Oil Company and executed by West Coast; however, the agreement was rejected by Midwest during the latter part of November, 1962. (R. 220; R. 2751-2780). As late as April

1963, Dickinson still thought Midwest might participate. (R. 220). Gay's efforts to obtain financing were unsuccessful but Magnuson was not aware of his activities, or the negotiations with Midwest until after Midwest rejected the deal. (R. 220; R. 1290).

The Booth Leasing Company had suggested to Gay that his financing efforts might be more successful if he obtained a guarantor. (R. 1635). Recalling Magnuson's earlier interest on behalf of Golconda Gay contacted him concerning interim financing and a guarantee from Golconda. Magnuson was told that West Coast was getting short of cash (R. 1765) and he agreed to supply some interim financing. On December 11, 1962, Magnuson sent a check to West Coast for $20,000 (R. 1409) and an additional $20,000 was loaned by him to West Coast on December 17, 1962. (R. 240). These loans subsequently were repaid by the issuance of 20,000 shares of West Coast stock to Magnuson at $2.00 per share during the Spring of 1963. (R. 240).

Magnuson attended the opening of the Downey installation on December 15, but he did not receive any financial information. (R. 1631). The Silver Buckle stockholders letter, dated December 7, 1962, was prepared without Magnuson's knowledge by Hull, Scott and Gay. (R. 2090-2096; R. 2139). Financial information for West Coast was not included. (R. 2092).

In early December, Scott also called Magnuson to inquire about Golconda's previous interest. (R. 1278). A

copy of each lease agreement was given to Magnuson to present to the Golconda board of directors, along with a long-term cash projection prepared by Ford & Wade, Certified Public Accountants, which projected a sizeable cash balance at the end of 1962 and larger cash balances at the end of 1963 and 1964. (R. 1279, 1280; see similar projection at R. 1446-1451). Golconda, subsequently, committed itself to guarantee West Coast's anticipated recourse obligations under the sale of these four leases up to a maximum of $420,000 in exchange for options to purchase West Coast stock and, as further security, the pledge to Golconda of the approximately two million shares of Silver Buckle stock previously obtained by West Coast. (R. 254). The Silver Buckle shares were deposited by West Coast in escrow at the Idaho First National Bank on December 11, 1962. (R. 258; R. 2991-2993). Silver Buckle also pledged to Golconda its remaining portfolio of mining securities and may have given Golconda a first lien on all its mining property, including the Vindicator project. (R. 254).

A third loan of $10,000 was made by Magnuson to West Coast on January 9, 1963, evidenced by a promissory note. (R. 273).

At Gay's request, a preliminary financial statement for Golconda, as of December 31, 1962, was forwarded to Gay on January 16, 1963. (R. 285). The leases were sold to Guthrie Investments, Inc., a Washington financing corporation, for $770,000 cash on January 28,

1963, with recourse against West Coast and Silver Buckle for any defaults in rent payments. (R. 288; R. 3058-3064). Jack Gay and Richard Cary, the attorney and Secretary for West Coast, executed the agreement on behalf of West Coast. Gay said that this sale would cover West Coast's long term financial needs. (R. 1323). The Bank of California purchased the paper from Guthrie and Golconda pledged 20,000 shares of Lucky Friday stock to the Bank in furtherance of its guarantee. (R. 288). At this time Magnuson and the Golconda directors received summaries of the financial information on the four lessees. (R. 288). The financial information referred to a date prior to August 13, 1962. (R. 3186-3188).

Golconda loaned West Coast $20,000 for additional interim financing on January 24, 1963. (R. 287). Ford & Wade prepared an exhibit of proposed installations and earnest money deposits; $38,600 earnest money deposits were received prior to January 31, 1963, $8,400 between January 31, 1963, and the preparation of the schedule, and $4,860,000 worth of leasehold contracts were shown. (R. 1678). Seven installations of 24 lanes each were anticipated to open between July 15 and December 1, 1963. (R. 3033).

The West Coast directors knew that their attachment to Silver Buckle, a mining company, was detrimental to the financing efforts of West Coast. Consequently, various merger and spin-off proposals were being considered during the spring of 1963 for the purpose of

isolating the mining properties of Silver Buckle. Magnuson was interested mainly in the mining properties of Silver Buckle and was not favorable to merger considerations. At various times his advice was sought as a professional accountant, but he was not involved in detailed discussions of the merger arrangements. (R. 1746, 1747). Magnuson was not being furnished financial information during March, April and May of 1963 and he was not involved in any detailed discussion of the finances of West Coast (R. 1757). Gay felt that the leases were delinquent, due to organizational problems, and he did not consider them in default. (R. 1747).

The West Coast 1962 Annual Report was issued February 28, 1963 with a financial statement for the period ending that date. (R. 298; R. 3287-3306). (Appendix, page 65). J. A. Hogle & Company (now Goodbody) became interested in underwriting an offering of West Coast stock (R. 301), and Gay informed M. Elwood A. Crandell, Hogle's underwriting manager, of the financing and merger plans of West Coast on March 26, 1963. (R. 3323-3325). Pacific Northwest Company had declined to act as underwriter on March 7, 1963. (R. 3320). Magnuson learned of the terms of the proposed merger on about March 27, 1963; he also discussed the financial problems of West Coast, the need for cash, and the "bogging down" of the prospective archery installations with Gay, Dickinson, Cary and Ford, the C.P.A. (R. 306). Magnuson's merger suggestions were not followed. (R. 306). On

April 1, 1963. Magnuson requested to be advised of the approximate date of the opening of the next four or five installations. (R. 3339). On April 4, 1963, Gay, Scott and Magnuson met with Al Jama, a San Francisco real estate developer, who was involved in the Redwood City, California proposed lease; Jama agreed to put up $100,000 cash, obtain a line of credit of $300,000 for West Coast and become a director. (R. 309). Magnuson agreed to recommend that Golconda acquiesce in the merger if all the outstanding stock of Silver Buckle Mines, Inc. (a wholly-owned subsidiary to be formed to hold the mining properties), was pledged to Golconda to replace the approximately 2,000,000 shares of Silver Buckle which had been pledged in the Guthrie guarantee obligation. (R. 311).

The Merger of West Coast and Silver Buckle

Notice of the annual meeting of stockholders of both companies was sent about April 24, 1963, together with financial statements for both companies and the merger agreement. (R. 314; R. 3480-3523). Silver Buckle Mines, Inc. was incorporated on May 3, 1963 and all the assets of Silver Buckle Mining Co. were transferred to it in exchange for all its shares. (R. 322). The shareholders of West Coast approved the merger of Silver Buckle Mining Co. and West Coast on May 25, 1963. (R. 331). Glen Sherman, a Kennewick businessman, had been recruited to become President after the firing of Dickinson and Magnuson reluctantly became a director only to fulfill his promise to Sherman. Magnuson, Scott, Gay, Jama, and Sherman

were the new directors. (R. 331). The new management felt that the removal of Dickinson as president would stop the excessive spending and it is further stipulated that the new directors thought the finance, sales and operations problems could be solved. (R. 333, 334). During February through April, 1963, the leases had shown that they could produce substantial operating revenues. (R. 333).

The merger took place on June 10, 1963; the stock of West Coast was split into 2½ shares of new, no-par stock and Silver Buckle shareholders received one share of the new stock of West Coast in exchange for 5 shares of Silver Buckle stock. (R. 331; R. 336). The old Silver Buckle stock was surrendered and cancelled. At a special meeting of the board on June 11, 1963, each director received a current operating statement for West Coast. (R. 338; R. 3555-3559). The balance sheet showed a cumulative deficit of $334,657.32 and the profit and loss statement showed a loss of $37,521.-56 for the month of May; net profit for the first five months of 1963 was $76,498.10. (R. 338).

About May 31, 1963, Silver Buckle loaned $25,000.00 to West Coast and, about the same time, Scott and Magnuson jointly loaned West Coast $20,000.00. (R. 335).

Trading Activity by Pennaluna and Harrison

Throughout this period of time, Pennaluna, through Harrison, was engaged in its normal trading activities. Pennaluna does not publish its quotations in any news

media and it does not place quotations in the so-called "sheets" operated by the National Quotation Bureau, Inc. (R. 210). Its bids and offers for Silver Buckle stock during 1962 and the first half of 1963 are shown on the schedule at pages 2438-2447 of the Record. These quotations sheets were correlated into a composite quotation sheet distributed to the news media and to the SEC for each trading day. (R. 210). Pennaluna generally was the highest bidder for Silver Buckle stock as well as other mining shares sold on the Spokane over-the-counter market. During the months following the New Park-East Utah transaction, Pennaluna's bids frequently were matched by J. A. Hogle & Company. For instance, on October 2, 1962, J. A. Hogle bid 1½c higher than Pennaluna; it matched Pennaluna's bid on October 10 and exceeded the bid by 1c on October 15. (R. 2442). The respondent has summarized the schedule and states in its findings and conclusions that Pennaluna was the single high bidder on only 34 days out of 56 days upon which Pennaluna and one other firm submitted bids during this period. (R. 4614). The national stock summary for the period October 1, 1962 through April 1, 1963 lists 24 companies who were making a market in the stock of Silver Buckle during that period; Pennaluna is not one of the firms listed. (R. 2448).

From October 1, 1962 through January 8, 1963, the respondent finds that the bid quotation and the subsequent market price throughout the nation rose steadily from 22c to a high of $1.40. (R. 4614). A schedule

showing transactions in the stock of Silver Buckle by the 32 broker-dealers most active in this stock for the period September 1, 1962 through December 4, 1962 is found at page 2938 through 2940; the Record also contains a schedule of all transactions in Silver Buckle stock by 92 broker-dealers during September and October, 1962. (R. 2941-2986).

The trading volume shown on these schedules for the period September 1, 1962 through December 4, 1962 was 2,512,462 shares; Pennaluna confirming as principal in all transactions bought 532,600 shares and sold 562,205 shares during this period; J. May & Co. (New York), R. E. Nelson & Company (Spokane, Washington), J. A. Hogle & Company (Spokane and national offices), Cromer Brokerage (Salt Lake City, Utah), Wallace Brokerage (Wallace, Idaho), and Ingalls & Snyder (New York, all had purshases or sales in excess of 100,000 shares. (R. 2938- 2940). 44 percent of Pennaluna's transactions between March 1962 and June 5, 1963, were with Harris Upham, Walston Company (Seattle and Pasco), Dean Witter & Company, Davidson (Great Falls, Montana), Merrill Lynch, Pierce, Fenner & Smith, and Bache & Company. (R. 883).

Pennaluna communicated with broker-dealers outside the City of Spokane by teletype. Of the hundreds of teletype conversations that took place during this period, the respondent contends that less than 10 such conversations with J. May & Company (New York),

Walston and Company (Seattle) and E. E. Smith reflect the alleged manipulative scheme. Generally, these conversations discussed current market activity in Silver Buckle stock and reflected Harrison's opinion concerning future activity and price. In these conversations, Harrison did not disclose that Pennaluna had directly or indirectly acquired a block of Silver Buckle stock from New Park or East Utah. (R. 257).

It is stipulated that Harrison's predictions concerning the price of Silver Buckle and other mining securities were based upon his experience as a trader and his skill in the business predictions of the price of mining shares to the same extent that other broker-dealers customarily engaged in such predictions. (R. 214; R. 890). It is further stipulated that, in connection with such predictions, Harrison had received no non-public information at any time about West Coast or Silver Buckle from Magnuson, and that these predictions were made without the benefit of any current financial information concerning Silver Buckle or West Coast. (R. 215) (Appendix, page 9).

Indicative of the nation-wide interest in Silver Buckle are the research and predictions made by Walter Faubion, a registered representative of Walston & Company. On November 30, 1962, Faubion teletyped Walston's research office in New York that he did not see any reason why the stock of Silver Buckle should not go to around $5.00. (R. 954, R. 956). A copy of this teletype was sent to Pennaluna by Faubion with

a request to buy 200 Silver Buckle shares for a customer. (R. 955). Harrison was also authorized to post the teletype on Pennaluna's bulletin board. (R. 955). Faubion continued his enthusiasm in a letter to Mr. D. J. Cullen, Vice President of Walston. (R. 3049). A copy was sent to Magnuson, together with a copy of Faubion's notes and price predictions. His final price prediction for Silver Buckle was $25 by January 1, 1965. (R. 1484-1488). Faubion also assisted West Coast in its financing efforts. (R. 2996, 3000). Further evidence of the interest of other broker-dealers is shown by a brochure on Silver Buckle prepared by G. Everett Parks & Co. Parks recommended the purchase of Silver Buckle shares, although not referring to the company by name, and referred to his firm's detailed study of Silver Buckle. (R. 251; R. 2924).

West Coast's archery equipment was publicized as a part of a TV show presented by ALCOA on January 31, 1963; at least 500 persons and firms were notified by West Coast, including many broker-dealer firms and financing houses, and the show received wide-spread advance publicity. (Scrapbook II, page 12). There also was a report on January 7, 1963 in the National Observer, a Dow-Jones publication. (R. 277) (Scrapbook II, page 12). An article on West Coast appeared in the Wall Street Journal on March 21, 1963, referring to $5 million worth of equipment used by archery lanes. This figure was furnished by West Coast (R. 312) and was based upon various letters and down payments received from interested persons during

the fall of 1962 and the first part of 1963. (R. 3349-3473). There was a second article on the Downey Archery Lanes in the Wall Street Journal on April 18, 1963. (R. 312; R. 3348).

West Coast's Activity After the Merger

About May 13, 1963, Midnite Mines, Inc., a substantial mining company, obtained shareholders approval for an exchange of stock with West Coast which would give West Coast about $500,000 of additional borrowing strength; the stock exchange did not take place. (R. 333).

The Bank of California, as Guthrie's assignee, knew the status of the rental payments on the Portland, Downey and Covina installations which had become delinquent. (R. 324). Despite this knowledge, the Bank of California made three unsecured loans to West Coast of $50,000 each on May 22, 1963, June 27, 1963, and July 17, 1963. (R. 324). On October 23, 1963, Guthrie Investments, Inc. purchased the lease for the Redwood City archery lanes. (Redwood City became operative in December, 1963. (R. 334)). Both Guthrie and the Bank of California felt that West Coast's problems were the result of normal growing pains, including the lack of operating capital on the part of the lessee and lack of a full season for operation. (R. 325).

Despite the difficulties with the archery ranges and large expenditures for promotion and overhead, West Coast still had a net profit for the first six months of

1963 of $45,429.28. (R. 345; R. 3565-3569). Because of a loss in July, the first seven months of 1963 showed a net loss of $4,689.12. (R. 355; R. 3590-3594).

From August 14, 1963 through December 31, 1963 Magnuson sold 29,351 shares of West Coast stock, both for his own account and his children's accounts for which he acted as custodian. (R. 430). These shares had been purchased during December 1962; the respondent's findings state that, of the 5,250 shares sold to Pennaluna during September, 1963, only 750 shares were resold. (R. 4612).

About September 1, 1963, Magnuson loaned West Coast $20,000 and Golconda loaned it $25,000. (R. 364). A further loan of $5,000 was made by Magnuson on September 24, 1963, convertible to West Coast stock at the rate of 80c per share; (R. 371) Magnuson provided West Coast with an additional $10,000 on October 12, 1963. (R. 379). In addition to this direct financing, Magnuson was assisting West Coast during the summer of 1963 by contacting publishers of financial reports, financing houses, and other broker-dealer firms.

In a letter to Sherman on September 26, 1963, Magnuson reaffirmed his confidence in the company and the progress made by Sherman; he stated that with an additional $200,000 of financing, West Coast would have a bright and successful future; these expectations were based in part on the efforts of Jama to obtain a

line of credit for the company. (R. 3620). On October 12, 1963, Magnuson reported a conversation with Guthrie to Sherman; he stated that Guthrie would purchase the Jama lease (Redwood City) and that the Bank of California was not concerned about West Coast's finances. (R. 3628).

Mineral Exploration Company, an affiliate of the Vinnell Corporation, was interested in the Silver Buckle mining properties. (R. 404). Mel Redhead, a geologist employed by Mineral Materials, Inc., also was doing a field examination of the Vindicator and Silver Buckle properties for his company. (R. 391; R. 3628). A favorable geological report was submitted later that fall. (R. 404; R. 3647, R. 3648). On October 15, 1963, Sherman recommended that West Coast sell only on a cash basis, F.O.B. Seattle; he also advised a person inquiring about West Coast stock to contact Ray Moore, a representative of Bache & Company, a Seattle broker-dealer. (R. 380).

The Redwood City lease was sold to Guthrie on October 23, 1963 for $164,000; West Coast's recourse obligations were guaranteed by Magnuson and Golconda up to a maximum of $35,000 and $25,000 respectively. (R. 384). A complete resume of West Coast's financial problems was given to Magnuson by Sherman on November 6, 1963. (R. 3643).

The Brunswick Corporation had been investigating West Coast's archery business during October, November and early December 1963; before Christmas

of 1963, the directors of Brunswick decided against entering the archery business. Brunswick reported to Magnuson that it recognized the potential of archery but felt that it would take five years and approximately $12,000,000 to develop the market. (R. 399). Golconda was required to make a payment of $42,241.12 to Guthrie and California tax authorities; pursuant to its guarantee obligations; on January 8 and 9, 1964, Golconda, as pledgee, sold pledged assets of Silver Buckle Mines, Inc. for reimbursement of this amount. (R. 411).

Pennaluna loaned $12,200 to West Coast for the purchase of certain claims of creditors in the fall of 1963. (R. 416).

On January 13, 1964 West Coast directors decided to discontinue the archery business, except for the completion of orders sold for cash to Kanematsu & Co., Ltd. a Japanese concern. (R. 412; R. 3228-3260). A public offering of the shares of Silver Buckle Mines, Inc. pursuant to the regulation A exemption from Section 5 of the Securities Act of 1933, was being considered at this time; Richard Cary met with Mr. James E. Newton, Regional Administrator of the respondent, concerning this offer on or about February 21, 1964. (R. 3698). Magnuson resigned as a director on February 21, 1964 on the advice of his attorney Alden Hull. (R. 3700).

Although Magnuson was no longer an officer or director of West Coast after April, 1964, Magnuson

loaned an additional $80,000 to West Coast for the purchase of claims and the payment of administrative expenses, guaranteed an obligation of Silver Buckle to Guthrie to the extent of $100,000 and agreed to indemnify the liquidating trustee of West Coast against certain contingent and disputed claims. (R. 417). These guarantees by Magnuson and other shareholders freed the stock of Silver Buckle Mines, Inc. from the pledge to Golconda for distribution to shareholders and creditors of West Coast. (R.417).

Since automated archery was not being accepted by the public, despite the substantial improvement by the lessees in the Spring of 1963, the directors of West Coast decided to place the company in a voluntary receivership. The notice, letter, and plan of liquidation are found at page 94 of the Appendix Over 80 percent of the outstanding stock was voted in favor of liquidation at the shareholders meeting on March 19, 1965. (R. 417). Approximately 5,000,000 shares of the outstanding stock of Silver Buckle Mines, Inc. were distributed to the shareholders of West Coast as a liquidating dividend and the shares of Silver Buckle Mines, Inc. now are actively traded. Magnuson and Pennaluna received 733,333 shares and 81,333 shares respectively. Magnuson paid $100,000 to Guthrie and received 1,000,000 shares. Guthrie also received 1,662,500 shares of Silver Buckle in satisfaction of that corporation's debt to Guthrie Investments, Inc. (R. 418). Magnuson's total investment exceeds $250,000. The final payment has been made to the liquidating trustee and all

liabilities of West Coast have been settled satisfactorily. (R. 4547).

At this time, Magnuson has no interest in Pennaluna either as an officer, director or stockholder, and is not engaged in the securities business in any manner.

III.

SPECIFICATION OF ERRORS AND QUESTIONS IN THE CASE

A. Whether or not there is substantial evidence in the Record to support the respondent's finding that petitioners failed to establish that the shares of Silver Buckle purchased and sold were exempt from the registration requirements of Section 5 of the Securities Act of 1933.

1. Did the respondent place the burden of proof upon the proper party and did the respondent properly apply the standard and quantum of proof required?

2. Did the respondent consider only material evidence contained in the Record and properly evaluate and give weight to evidence supporting petitioner's contention?

3. Do the respondent's findings comply with its obligation to present specific, detailed factual conclusions particularly with reference to its finding of a viola-

tion of Section 5 of the Securities Act by each petitioner on a different basis?

4. Does the order denying reconsideration contradict the respondent's previous findings and opinion by stating that Oil, Inc. was not a member of a control group?

B. Whether or not there is substantial evidence in the Record to support the respondent's finding that each petitioner violated Section 10(b) of the Securities Act and Rule 10(b)6 promulgated thereunder.

If the shares involved are exempt from registration and a special selling effort is not present, upon what basis can the respondent find that the necessary distribution was taking place?

C. Whether or not there is substantial evidence in the Record to support the respondent's finding that each petitioner was engaged in a manipulative scheme in the sale of stock of Silver Buckle Mining Company and West Coast Engineering, Inc. contrary to the provisions of Section 17(a) of the Securities Act and Sections 10(b) and 15(c)(1) of the Securities Exchange Act and the rules promulgated thereunder.

1. Can less than ten TWX conversations made by Pennaluna over a substantial period of time sufficiently establish that a manipulative scheme was present in the absence of excessive bidding and trading in the stock of Silver Buckle?

2. Do the respondent's findings contradict the stipulation that it was Magnuson's policy not to give Harrison non-public information:

(a) By concluding that improper price predictions were made;

(b) By concluding that certain statements were misrepresentations materially affecting the market activity for Silver Buckle stock;

without finding that the above policy was not followed with regard to Silver Buckle stock?

3. Upon what basis does the respondent find that Harrison had a duty to discover and subsequently disclose financial information concerning West Coast Engineering, Inc. and further charge Harrison by implication with a responsibility for the activities of West Coast's management?

4. Does the respondent's finding that there was no tangible basis for belief in the financial solvency of West Coast during August, 1963 constitute an arbitrary and capricious disregard of legitimate efforts to obtain the necessary financial assistance?

D. Whether or not the Division of Trading and Markets purposely led the petitioners into a belief that a sanction of suspension of a certain number of days would be forthcoming from the respondent, which representations and inducements caused petitioners to

present a stipulated record appropriate only for documentary evidence.

Did respondent's staff purposefully exclude exculpatory and mitigating material from the Record and further conduct the proceedings contrary to the intent and purpose of the Administrative Procedure Act?

E. Whether or not the sanction imposed by respondent constitutes an arbitrary and capricious abuse of respondent's discretionary enforcement powers.

1. Did the respondent properly consider opinions and material supporting the character and integrity of petitioners and Pennaluna's valuable function in the Spokane Stock Exchange and the over-the-counter market?

2. Did the respondent properly evaluate remedial efforts undertaken by petitioner Pennaluna and present compliance by Pennaluna with the record keeping and accounting rules of the respondent and the Board of Governors of the Federal Reserve System?

By stipulation the petitioners have preserved their right to object to the relevancy or materiality of any evidence considered by the respondent. (R. 443). Because of the conclusory nature of respondent's finding and opinion, petitioners are unable to set forth in index form the exhibits presented, together with their admission or rejection. A simple index of the substantial number of exhibits in the Record would further en-

umber this brief, and would not aid this Court. Petitioners will emphasize and continue their objection o any immaterial or irrelevant evidence which may ave been considered by respondent.

IV.
ARGUMENT

The findings, opinion and orders of the respondent re not supported by substantial evidence. In construng the substantial evidence concept, this Court must onsider evidence in the Record fairly detracting from nd contradicting the evidence relied upon by repondent. The whole record must be considered. *Universal Camera Corp. v. N.L.R.B.*, 340 U.S. 474, 488, 5 L.Ed. 456, 467 (1951). The consideration of all maerial evidence and exhibits is critically important in his case, as improper inferences have been drawn by espondent from irrelevant facts.

Purchases and sales of Silver Buckle stock by petitioners during 1962 and by Pennaluna during 1963 were exempt from the registration requirements of Section 5 of the Securities Act (15 U.S.C.A. 77e); Magnuson was not a controlling person or a member of group in control of Silver Buckle during 1962 and arly 1963 and Pennaluna did not purchase Silver Buckle shares from Magnuson in the Oil, Inc. and New Park transactions. The respondent has disrearded the basic elements of the control concept.

The alleged misrepresentations made to other brokerealers by Harrison in less than 10 TWX conversa-

tions cannot support an inference of a manipulative scheme, since this "broker's chatter" could not have had a substantial effect upon the rise in price of a stock caused by nation-wide publicity and brokerage activity. The financial success of a developing company can be determined only over a long period of time; it is improper for the respondent to emphasize current difficulties without giving weight to the possibility of long-term success, particularly when a manipulative scheme is alleged. The "whole record" indicates that there was no violation of the anti-fraud provisions of the Acts by any petitioner.

The Division of Trading and Markets purposefully induced petitioners to present the matter to the respondent on stipulated facts, a posture of the case appropriate only for a sanction of suspension or censure. Because of the nature of the administrative process, petitioners must be informed of the exact sanction sought by the staff. Revocation is discretionary, and petitioners otherwise are unable to appreciate the severity of the allegation. If petitioners had known that revocation rather than suspension was the goal of the staff, a hearing would have been requested, at which the demeanor of the witnesses could be considered and more detailed findings made by an examiner.

Petitioners further request this Court to determine that the sanction imposed upon petitioners is a clear and dangerous abuse of the respondent's discretionary enforcement powers.

THE RESPONDENT'S FINDING THAT THE SILVER BUCKLE SHARES PURCHASED AND SOLD DURING 1962 AND 1963 BY PETITIONERS REQUIRED REGISTRATION UNDER SECTION 5 OF THE SECURITIES ACT (15 U.S.C.A. 77e) IS NOT SUPPORTED BY SUBSTANTIAL EVIDENCE.

A. The respondent required petitioners to establish an exemption from registration; under the circumstances of this case, placing the burden of proof upon petitioners constitutes an abuse of administrative due process of law.

Sale of the Silver Buckle shares purchased by Magnuson and Pennaluna from Oil, Inc., in May, 1962 and New Park-East Utah on September 29, 1962 required registration under Section 5 of the Securities Act *only if* the selling party was a controlling person or a member of a control group. Section 2(11) of the Securities Act defines underwriter as including one who purchases from a controlling person; the presence of an underwriter in a transaction then places that transaction within the scope of the Section 5 registration requirement.[1] The respondent clearly placed the bur-

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1. Section 2(11) of the Securities Act (15 U.S.C.A. 77b(11) states as follows:

> "The term 'underwriter' means any person who has purchased from an issuer with a view to, or offers or sells for an issuer in connection with, the distribution of any security, or participates or has a direct or indirect participation in any such undertaking, or participates or has a participation in the direct or indirect underwriting of any such undertaking; but such term shall not include a person whose interest is limited to a commission from an underwriter or dealer not in excess of the usual and customary distributors' or sellers' commission. As used in this paragraph the term 'issuer' shall include, in addition to an issuer, any person directly or indirectly controlling or controlled by the issuer, or any person under direct or indirect common control with the issuer."

den upon petitioners to prove by a preponderance of the evidence that the controlling person and underwriter concepts were not present. Although petitioners feel they met this burden, to require them to do so still disregarded the constitutional protections of the administrative process.

We are concerned not with a simple fact issue but with a much more difficult problem of rebutting a presumption. Purchases from an issuing company carry a presumptive need for registration, and, since this need should be apparent, it is consistent with administrative due process to require a seller or purchaser to establish that an exemption is present. To place this presumption upon non-issuers is not equally consistent. Rebuttal of a presumption requires much more than the mere preponderance of the evidence. Since the Division is the proponent of the claimed need for registration, the Administrative Procedure Act states that the Division shall bear the burden of proof. 5 U.S.C.A. 556(d).

S.E.C. v. Ralston Purina Company, 346 U.S. 119, 126, 97 L.ed. 1494, 1499 (1953) stated that:

> "Keeping in mind the broadly remedial purposes of federal securities legislation, the imposition of the burden of proof on an issuer who would plead the exemption seems to us fair and reasonable."

The Supreme Court was concerned with a primary distribution from the issuing company, not a secondary

distribution from allegedly controlling persons. Later cases like *S.E.C. v. Culpepper,* 270 F. 2d 241 (2nd Cir. 1959) and *Gilligan, Will & Company v. S.E.C.,* 267 F. 2d 961 (2nd Cir. 1959) involved a sale by the issuing company through the conduit of controlling persons. Consequently, the cases are not binding upon this Court.

That administrative due process of law has been abused is illustrated by the three successive theories of control presented by the Division.

(1) During the deposition of Dr. F. E. Scott, the investigating representatives of the Division contended that New Park and East Utah had sufficient stock, (being approximately 1,400,000 shares) to control Silver Buckle and that the subsequent purchases by Magnuson and Pennaluna from those companies consequently required registration. (R. 2016).

(2) Recognizing that New Park and East Utah were in opposition to the management of Silver Buckle and therefore unable to assert a controlling influence, the Division in its brief then attempted to establish an involved business and social relationship between Magnuson, Harrison and directors of Silver Buckle. (R. 3764-3768; R. 3921-3928).

(3) Faced with a comprehensive rebuttal of this allegation by petitioners in their brief, (R. 4007-

4020) the Division then asserted that Oil, Inc., itself, was a member of the so-called group in control of Silver Buckle for purposes of establishing a need for registration of shares acquired in the Oil, Inc., transaction and subsequently sold. (R. 4433).

This last allegation was successfully rebutted in petitioner's supplemental brief; (R. 4517) the respondent has found in its order dated July 6, 1967 that Oil, Inc. was not a member of a control group in May, 1962. (R. 4662; Appendix page 124). Respondent apparently has concluded that only Scott and Magnuson were controlling persons — a contention not raised by the Division and therefore not directly dealt with by petitioners. (R. 4612; Appendix page 112).

Even assuming that this is an adversary proceeding, this constant change of position by the respondent and its staff indicates the need for this Court to establish a new standard for the burden of proof and to effectively clarify the scope of *S.E.C. v. Ralston Purina, supra.* When sellers of stock are not the issuing company and have legal opinions and other evidence indicating that the sellers (whether it is Magnuson or the selling companies) do not have a control status with the issuer, the respondent's staff must bear the burden of proof, if it seeks to challenge a prima facie exemption from registration. The concept of burden of proof is a judicial standard which must be interpreted to fit the needs of a particular situation. This

question should be remanded to the respondent for further findings consistent with a proper allocation of the burden of proof, and recognition of the respondent's administrative obligations.

B. The "whole record" does not support the respondent's finding that Magnuson was a member of a control group during the entire period under review; the respondent further has failed to make responsible, specific findings.

I Loss, *Securities Regulation*, 2nd edition, page 557 states the accepted test for determining a control status under Section 2(11) of the Securities Act (15 U.S.C.A. 77(b)(11)) as follows:

> "Is a particular person in a position to obtain the required signatures of the issuer and its officers and directors on a registration statement? No other criterion would do, since the controlling person himself is not an 'issuer' except for the purpose of Section 2(11)."

Despite substantial and conclusive evidence to the contrary, respondent, apparently, concludes that Magnuson had this power at all times from May, 1962 through July, 1963. The respondent states that

> "It appears that throughout the period when Silver Buckle's stock was being distributed, as described above, Magnuson and Scott were in effective control of Silver Buckle and by various arrangements and with the assistance of Harrison and the younger Cranmer were able to arrange for the acquisition of large blocks of Silver Buckle stock by friendly hands or for its disposition to new owners who would not pose the threat to the market indicated by Steen." (R. 4612; Appendix page 112).

The "period" referred to included two separate transactions and it is incumbent upon the respondent to make a responsible finding and conclusion for each transaction. *S.E.C. v. Chenery Corp.,* 318 U.S. 80, 94; 87 L.Ed. 626, 636 (1943). There must be a finding concerning the selling party in each transaction and the facts bearing upon the presence or absence of a controlling status at the time of acquisition or sale. To simply rely upon appearances violates the respondent's obligation to set forth specific, responsible findings. *S.E.C. v. Chenery Corp., supra.*

1. The Oil, Inc. Transaction.

The details of this transaction are set forth on pages 13-16 of this brief, and a schedule of the purchases is found on page 2 of the Appendix. Magnuson owned 542 shares of Silver Buckle stock and had no connection with Silver Buckle prior to May, 1962. The respondent admits that Oil, Inc., the seller, was not a member of a group in control of Silver Buckle and that Scott arranged the transaction using Magnuson's name and account only to implement an escrow agreement. (R. 4610; Appendix page 110) Magnuson became involved in the transaction solely because of his interest in silver and because of his reputation for investments in mining ventures; (R. 1138, 1139). All purchases were made without any financial information. (R. 1145). Since Pennaluna had resold its 90,555 shares in the normal course of trading by July 14, 1962, its participation in the transaction was completed long

efore the second purchase occurred on September 29, 962. (R. 2395, 2396; R. 4610).

If respondent does not accept the substance of the ransaction, it is incumbent upon it to make a finding o that effect. Under the circumstances, the shares urchased and sold by both petitioners were exempt rom registration under the provisions of Section 4(1) f the Securities Act. (15 U.S.C.A. 77d(1)).[2]

. The New Park Transaction.

Magnuson had no contact with Scott and Silver Buckle during the summer of 1962, prior to the Ruby Silver Mines dispute. (See page 16, 17 of this brief) He held less than 2 percent of the issued and outstanding stock of Silver Buckle and was not an officer or irector of the company. In order to protect Pennaluna nd a public offering of the shares of Ruby Silver Mines, Inc., Magnuson arranged the meeting that resulted in the two contracts between the companies and Silver Buckle and between the companies and Magnuson as the record purchaser. The respondent's findings state that Scott and Pennaluna had agreed to purchase 300,000 shares and 200,000 shares respectively rior to the transaction. (R. 4610; Appendix page 110). That the companies are the selling parties should be bvious; each purchaser made his payment in to the Magnuson escrow account and received a certificate epresenting his proportionate interest in shares for-

2. Section 4(1) of the Securities Act of 1933 exempts transactions by any person other than an issuer, underwriter or dealer from the registration requirements of Section 5 of the Securities Act.

warded to the escrow agent by New Park and East Utah. (R. 2609). The use of the Magnuson account for escrow purposes by the Spokane National Bank, rather than opening a separate account, should be completely irrelevant. The respondent, however, still avoids this question by refusing to make a specific finding as to the selling party for shares acquired by Pennalua and other purchasers. The details of the transaction are set forth on page 18-20 of this brief; the schedule of purchasers is found on page 4 of the Appendix.

Whether the 365,000 shares purchased by Magnuson in this transaction required registration prior to sale must rest first upon facts in existence at that time. The subsequent guarantee and financial assistance to West Coast by Golconda and the loans by Magnuson during December, 1962, have no bearing upon Magnuson's status as a member of a control group on September 29, 1962. The Golconda guarantee of West Coast's obligation did not become binding until January 28, 1963, the date of West Coast's sale of its lessor's interest in Denver, Portland, Downey and Covina leases to Guthrie Investments, Inc. (R. 288; R. 3058-3064). Only Golconda's interests were being protected by Magnuson as is conclusively demonstrated by the limited guarantee and by the pledge of Silver Buckle shares and Silver Buckle securities portfolio as security. (See page 27 of this brief). The first loan by Magnuson was made on December 11, 1962 (R. 240). There is no evidence that he had any financial information or exercised any influence whatsoever upon Silver Buckle or West Coast

prior to late April, 1963. To say that "beginning in late, 1962, Magnuson became deeply involved in the affairs of West Coast" is a gross distortion of the facts, in addition to being completely irrelevant to his status on Septembr 29, 1962. (R. 4611; Appendix page 111). These inferences cannot possibly affect Pennaluna's purchase from New Park-East Utah.

The respondent further finds that Harrison and Pennaluna, although purchasing 100,000 shares for Pennaluna directly from New Park and East Utah (non-controlling persons), sold for or on behalf of a controlling person in violation of Section 5 of the Securities Act. (15 U.S.C.A. 77e) (R. 4612; Appendix page 112). Resale of these shares was completed on or about December 5, 1962. (R. 2411). For these shares to require registration the respondent must believe, although it did not specifically find, that Magnuson was a controlling person during October, November and December, the period of sale. Under the circumstances, Harrison did not know or have reason to know of any facts leading him to believe he might be an underwriter. Not even the respondent can find enough facts to make a specific finding.

On January 10, 1963, representatives of the Division of Trading and Markets told Magnuson that they were concerned about the possible status of New Park and East Utah as companies in control of Silver Buckle. (R. 278; R. 3014; R. 4613). Since that contention is no longer being raised and has been conclusively rebutted by the evidence in the record, the conversation

itself does not constitute any forewarning to petitioners of the subsequent action by the respondent. Legal opinions obtained by Silver Buckle and Magnuson from John Lee and Alden Hull, attorneys experienced in S.E.C. practice, have been fully substantiated by the respondent's findings. (See opinions on pages 5 and 7 of the Appendix). Therefore, Harrison and Pennaluna, in particular, were entitled to rely upon those legal opinions. This is not a breach of promise suit; petitioners were entitled to make their own determination concerning the need for registration of the shares they acquired and sold. Petitioners continue their objection to reliance upon this discussion for any probative purpose, since it is immaterial and irrelevant. (Objection Preserved, R. 443).

Certificates representing the second 100,000 shares purchased by Pennaluna had been placed in a special envelope and charged to the drawing account of Harrison and Magnuson on or about January 12, 1963, on a 62½-37½% basis, as a result of the discussion with the Division's representatives; this was only a good faith effort to cooperate with the respondent during its investigation of the rise in price of the stock of Silver Buckle. Having determined that the basis for the discussion was not accurate, and further relying in part upon the Silver Buckle letter to brokers on March 5, 1963 (See Appendix page 86), the 100,000 shares were sold to Pennaluna through the account of Jerry O'Brien. These shares then were sold by Pennaluna in the normal course of its trading activity from May 2,

1963 through July 17, 1963. (R. 2434-2437). Tax considerations and other factors motivating this transaction are discussed at page 21 of this brief. That petitioners did not contact the Division prior to the transaction has no probative value.

The shares attributable to Magnuson and sold by Pennaluna, as well as the 750 shares of West Coast purchased by Pennaluna, as well as the 750 shares of West Coast purchased by Pennaluna from Mary Magnuson (purchase price $1,387.50), on August 26-29, 1963, would qualify for the exemption for "broker transactions" set forth in Section 4(4) of the Securities Act (15 U.S.C.A. 77d(4)),[3] if Pennaluna had confirmed the transaction as agent rather than as principal. These shares were less than 1 percent of the outstanding stock of the issuers and the transactions would be within the definintion of "brokers transactions" set by Rule 154 (17 CFR 230.154) but for the fact that Rule 154 does not include principal transactions. (Other sales of Silver Buckle by Magnuson had been made through other broker-dealers, as it was Magnuson's policy not to trade through Pennaluna.)

We recognize that the respondent is not going to broaden the arbitrary limitations of its rule; however, we wish to point out to this Court that the presence

3. Section 4(4) of the Securities Act of 1933 states that the provisions of Section 5 shall not apply to "brokers' transactions executed upon customers' orders on any exchange or in the over-the-counter market but not the solicitation of such orders."

or absence of a technical violation of Section 5 of the Securities Act may turn on the manner in which the sale was confirmed rather than the substance of the transaction. As to the West Coast shares Magnuson further testified that he did not control his mother's account. Therefore, Pennaluna did not purchase the West Coast shares from a controlling person and the shares could be sold properly without registration.

C. Petitioners have established that a control group was not present as a matter of law; since the shares involved did not require registration, this Court should reverse and set aside the order.

> "The concept of control herein involved is not a narrow one, depending upon a mathematical formula of 51 percent of the voting power, but is broadly defined to permit the provisions of the Act to become effective wherever the fact of control actually exists." H. R. Rep. No. 85, 73rd Cong., 1st Sess. 14 (1933).

The "fact of control" actually did exist in *In The Matter of S. T. Jackson, Inc. et al.,* 36 SEC 631 (1950). In that case, six stockholders, holding almost 75 percent of the common and preferred stock of the company, had organized the company and were active in its management. There was only a negligible market for the common stock prior to 1946 and the six stockholders obviously began disposing of their stock as part of a general plan. There were close business and social relationships among all six members of the group so that they were a cohesive group organizing and running the affairs of the company.

In *Strathmore Securities, Inc. and Turner,* Securities Exchange Act Release No. 8207 (1966) the 19 stockholders of a small corporation were united by family, personal, or business ties, and acted at the direction of a single person. A joint participation by stockholders in a scheme to purchase shares to distribute to the public was present also in *S.E.C. v. North American Research Devel. Corp.,* 280 F. Supp. 106 (SDNY 1968); however, the court absolved three defendants who acquired their shares from a person no longer having a control status.

The factors uniting the groups in these cases are not found in this Record. Close business and social relationships did not exist between Magnuson and Scott. Until Magnuson became a director of West Coast, he had never been an officer, or 10 percent stockholder of West Coast or Silver Buckle. It is respectfully submitted that this Court should reverse and set aside the order on this issue, or, in the alternative, remand to the respondent for findings consistent with a proper allocation of the burden of proof.

SINCE A CONTROL RELATIONSHIP IS NOT SUPPORTED BY A CONSIDERATION OF THE WHOLE RECORD, A DISTRIBUTION WAS NOT PRESENT FOR PURPOSES OF RULE 10b-6.

Rule 10b-6 (17 CFR 240.10b-6) promulgated by the respondent to execute Section 10(b) of the Securities Exchange Act (15 U.S.C.A. 78j(b)) generally prohibits an issuer, underwriter or dealer, while par-

ticipating in a particular distribution, from bidding for or purchasing any security subject to distribution in the open market. The rule rests upon the presence of a distribution, a term not defined. The respondent admits that a special selling effort was not present (R. 4619; Appendix page 119) and the other customary criteria of a distribution were not present. (See, e.g. *Bruns, Nordeman & Company,* 40 SEC 652 (1961) and *In the Matter of Theodore Landau,* 40 SEC 1119 (1962). The respondent rests its finding of a violation solely upon its previous conclusion that Pennaluna was an underwriter in the Oil, Inc. and New Park- East Utah transactions and that Magnuson, by implication, sold shares during May, 1962 through June 1963 while a controlling person. (R. 4619; Appendix 119). Since the "whole record" does not support the threshold findings of control, substantial evidence does not support the finding of a violation of Rule 10b-6.

SUBSTANTIAL EVIDENCE DOES NOT SUPPORT A FINDING OF VIOLATIONS BY PETITIONERS OF THE ANTI-FRAUD PROVISIONS OF THE ACTS[4]

A. The respondent has failed to delineate the standard of proof applied by it as the trier of the fact.

The respondent does not state that the Division had the burden of proof. Assuming that this was recognized implicitly, the quantum of proof required by respondent is not stated. Misrepresentations are alleged which, if found, constitute fraudulent activtiy. A mere pre-

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4. Section 17(a) of the Securities Act provides in part:

"It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly —

"(1) to employ any device, scheme, or artifice to defraud,"

Section 10(b) of the Securities Exchange Act provides in part:

"It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange —

"(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may describe as necessary or appropriate in the public interest or for the protection of investors."

Section 15(c)(1) of the Securities Exchange Act provides:

"(c) (1) No broker or dealer shall make use of the mails or of any means or instrumentality of interestate commerce to effect any transaction in, or to induce the purchase or sale of, any security (other than commercial paper, bankers' acceptances, or commercial bills) otherwise than on a national securities exchange, by means of any manipulative, deceptive, or other fraudulent device or contrivance. The Commission shall, for the purposes of this subsection, by rules and regulations define such devices or contrivances as are manipulative, deceptive, or otherwise fraudulent."

ponderance of the evidence is not sufficient for the judicial process; petitioners are entitled to the same degree of protection in the administrative process. The so-called stipulation of facts does not present stipulated *ultimate facts;* it only sets forth a succession of facts and events. (R. 86-445). Consequently, the respondent had the responsibility to sift and consider; the degree of proof it was using in this process therefore is extremely critical. Respondent should require a greater standard of proof akin to the "clear and convincing" concept for the proof of fraud in common law actions. That the elements of common law fraud are not required for securities misrepresentations does not negate the burden of proof concept. Because of the severity of sanction that has resulted in this action, using only a preponderance of the evidence standard constitutes deprivation of property without due process of law.

It is respectfully submitted that this Court should remand the action to the respondent for a further determination of the standard of proof to be applied to this issue.

B. Since even the preponderance of the evidence does not establish manipulative activity, the respondent's findings and opinion are arbitrary and capricious; the "whole record" does not support respondent's conclusion.

The respondent has *not* found that:

> (1) Pennaluna and Harrison dominated the market for Silver Buckle and West Coast stock or controlled a disproportionate amount of stock;

(2) Nor that an artificial market was maintained;

(3) Nor that any purchases and sales were made at any price other than the prevailing market price, including sale of the shares acquired in the New Park-East Utah transaction on September 29, 1962;

(4) Nor that any special selling efforts were adopted.

The respondent simply concludes that Pennaluna's normal trading activity, when coupled with alleged misrepresentations in less than ten TWX conversations and bullish price predictions, contributed substantially to the increase in trading and rise in price. (R. 4614; Appendix page 114). By inference only is such increase in trading considered harmful. The alleged misrepresentations and price predictions were not sufficient to establish the manipulative scheme by themselves; the respondent had to combine them with admittedly lawful conduct.

The question then must be:

How and upon what basis could the respondent conclude that it was the allegedly improper conduct rather than the proper trading activity that substantially contributed to the increase in price? It is respectfully submitted that the adminstrative process still must establish a relationship akin to the common law con-

cept of "proximate cause" and that the requisite cause and effect can not be found in the respondent's findings.

1. Trading Pattern and West Coast Publicity

Prior to September 29, 1962, there is no finding of a manipulative scheme. (R. 4613; Appendix 113). Consequently, the transaction during May, 1962, in which Pennaluna purchased 90,555 shares of Silver Buckle from Oil, Inc. for sale to the public is not involved. There are no allegedly improper TWX conversations at that time or allegedly unjustified price predictions; the flurry of market activity at that time, apparently, was proper.

The respondent emphasizes Pennaluna's lack of activity in this stock during September, 1962. If the respondent examined the conduct of other brokers during this month, it would find that the market was dull or "thin" due to the large blocks being dumped on the market by New Park and East Utah through the Cromer Brokerage Co. of Salt Lake City, (the so-called Salt Lake stock). J. May and Co., a New York broker with substantial trading activity, had sold 2,000 shares at 17c on September 4, 1962. (R. 4550). It is also stipulated that Magnuson first learned of the dispute that led to the transaction about the middle of September. (R. 197). Pennaluna's commitment to purchase 200,000 shares was made a day or two before the sale was negotiated. Pennaluna's bidding and trading activity during September prior to

its purchase on September 29, 1962 is completely immaterial and could have no probative effect.

The opening of the Denver archery lanes during the week of September 29, 1962 obviously awakened the market. (R. 203; R. 2611). The extensive publicity campaign by West Coast began with the opening of the Burien archery range on September 1, 1961 and continued throughout the Fall of 1962 and the Spring of 1963. The Scrapbooks compiled by the company diagram the activity. (See pages 22-24 of this brief). See also the press kit and sales brochure with financial projections (Appendix, pages 15-64). Gay had always informed interested persons that an interest in West Coast could be obtained by a purchase of Silver Buckle stock. (See, e.g., Gay letter dated March 7, 1962 at R. 2315).

Respondent admits that this publicity stimulated investors demand for Silver Buckle stock. (R. 4614; Appendix page 114). Respondent does not contend that petitioners are responsible in any way for West Coast's operations or publicity. How was the respondent able to differentiate the effect of the publicity and widespread activity by other brokers from the allegedly improper activity of Pennaluna, Harrison and Magnuson?

On September 29, 1962, Pennaluna purchased 100,000 shares of Silver Buckle stock from New Park and East Utah. (See page 18 of this brief). An effort to accumulate inventory for legitimate selling purposes

at the lowest price obtainable is proper. *In the Matter of F. S. Johns & Company,* Securities Exchange Act Release No. 7972 (1966). Any alleged misrepresentation, therefore, must relate to the manner in which the shares subsequently were sold and their effect upon the market, not the means by which they were acquired.

From October 1 through December 4, 1962, Pennaluna did not have "by far" the greatest volume of trading, as the respondent concluded. (R. 4614; Appendix 114). Again, the volume of trading itself is immaterial and inferences can be drawn from the volume of trading consistent with lawful and unlawful theories. 92 brokers reported their transactions for September and October, 1962. (R. 2941-2986). Of 2,512,462 shares traded September 1, 1962 through December 4, 1962, Pennaluna bought 532,600 shares and sold 562,205; several other brokers also had a volume in excess of 100,000 shares. (R. 2938-2940). Hogle (Goodbody) reported a volume of 1,172,920 shares from September 1 - March 31, 1963. (R. 4314). Pennaluna is not listed as a market maker on the National Stock Summary for October 1, 1962 through April 1, 1963. (R. 2448; Appendix page 85). There was no so-called "handholding" between Pennaluna and any of these broker-dealers; no request was made to insert bids in quote sheets. During this entire period Pennaluna simply bought and sold in its customary manner.

The Securities and Exchange Commission believes that a typical feature of market manipulation is a

rise in quotations without any demand for the stock. *F. S. Johns, supra.* This typical feature is not present. A comparison of the daily volume with the rise or fall in the Pennaluna bid on the following day shows a direct correlation between demand and price. Although Pennaluna always has been a high bidder, J. A. Hogle & Co. (now Goodbody) bid 1½c higher than Pennaluna on October 2, 1962, (R. 2442) the very next day after Pennaluna's improper-by-inference increase in its bid on October 1, 1962. (R. 4614). Hogle matched Pennaluna's bid on October 10 and again exceeded it by 1c on October 15. (R. 2442).

Consequently, Pennaluna's pattern of conduct during this period was quite normal and not designed to facilitate a manipulative scheme.

2. The TWX Conversations

The TWX conversations referred to in the respondent's finding at page 4615 of the Record have been set forth in full in the Appendix for the convenience of this Court. On October 4, 1962, Harrison had a TWX conversation with Anthony Vaghi, the trader for J. May & Co., (a market maker in Silver Buckle stock) (Appendix page 101). Harrison stated, among other things, that an agreement had been reached with New Park and East Utah. His prediction that Silver Buckle would be 65 "one of these days," by stipulation, was based upon his experience as a trader, and information that he had picked up "on the street" about Silver Buckle and West Coast. (See stipulation at

page 9 of the Appendix). Harrison had not received any non-public information or current financial statements. (R. 214, 215). Harrison also testified that George Hiltmyer, a representative of Harris, Upham and Company in Spokane, told him how good West Coast was going to be. (R. 217). An article about the transactions appeared in the Wallace Miner on October 11, 1962. (R. 222; R. 2823).

Throughout this proceeding petitioners have felt that respondent and its staff did not understand the manner in which mining securities are traded in the Spokane over-the-counter market and the factors that affect investment judgment. The TWX conversation on October 10, 1962 between Harrison and Walston & Co.'s Seattle office illustrates this point. (Appendix page 102). Harrison's statement that he "sees some very good inside buying on (Silver Buckle)" is one of the misrepresentations found by the respondent. (R. 4615; Appendix page 115). The Special Study of the Securities Market, Part 2, Chapter VII, states that the "inside" price is the price used by wholesale traders. The above TWX conversation refers simply to activity by "inside" buyers or wholesalers. (See also Vaghi testimony at R. 4490 in which Vaghi used the term). A trade term can not be the basis for any wild inference of a scheme or deal between Harrison and Walston. Selection of this conversation shows a gross lack of "administrative expertise" by respondent.

On October 26, 1962, Harrison stated to Vaghi again that Silver Buckle was headed for $1.00. (R. 238; Ap-

pendix page 103). This statement was not based on any financial information or non-public information but was based upon reports from Seattle brokers and the general trend of the market. Harrison frequently talked with the Portland office of Walston. The Special Study, Part 2, Chapter VII, page 557, points out that trading decisions often depend upon intuition and a feeling for the market.

On November 10, 1962, Harrison told E. E. Smith & Co., that Silver Buckle was going to sell much higher. (Appendix page 104). The TWX conversations on October 19 and December 10, 1962, with Vaghi referred to the previous blocks of Silver Buckle being sold by Cromer Brokerage which the New Park-East Utah transaction took off the market. (Appendix page 103, 104). The candor with which Harrison stated that he was making a low quote to accomodate Salt Lake certainly belies any manipulative scheme.

On February 8, 1963, Vaghi asked if West Coast was showing a monthly profit. (R. 295; Appendix page 105). Harrison did not know or have access to financial information not available to other brokers. If, in fact, he had seen a financial statement for West Coast for the eleven months ended January 31, 1963, he would have seen net earnings for that period of $43,711.18 and a reduced deficit for the company. (R. 3261).

During this period Harrison was not a controlling person or an insider; nor was he the partner of a person having that status. As shown above, Magnuson's

contacts with the management of Silver Buckle and West Coast were peripheral until late April, 1963. Each statement responded directly to the question within the limits of the communication and the disclosure obligation of Harrison. For instance, Harrison accurately reported that a large block of stock was no longer available to depress the market; it was not incumbent upon Harrison to go further and reveal that Pennaluna had purchased a small percentage. Pennaluna's shares were absorbed in and out of his trading account without any depressing effect upon the market and the remaining shares were tied up by the escrow agreement for the next few months. Within standards known and understood by wholesale traders, Harrison complied strictly with his obligations.

Vaghi stated this standard in part when he testified that he relied only upon buy and sell orders to make his market. (R. 4487, R. 4499). He did not seek financial information and looked to Harrison as a source of *broker's* information, (similar to the type Harrison received from Hiltmyer) not special, inside information. Vaghi did not know or care about Magnuson's alleged relation with Harrison and West Coast.

A mining security like Silver Buckle does not trade on the basis of financial information; despite its union with West Coast, Silver Buckle still traded like a mining security. Options to buy Silver Buckle stock were given to G. Everett Parks (a New York broker) by Magnuson during October and November, 1962;

(R. 235) it is quite significant that Parks did not request any financial information before making his commitment. (R. 1260). Petitioners submit that this is another factor which the respondent refuses to understand or believe.

Harrison did not have the financial information referred to by the respondent in its finding on page 4616. (Appendix page 116).[5] To imply that he had this information violates both the facts in the Record and the overall stipulation that Magnuson (assuming he had such information) did not provide Harrison with any non-public information. (Appendix page 9-14).

The Division continually disregarded this stipuluation but petitioners felt that the respondent would not be influenced by obviously improper argument. Before the Commission, Mr. Lane Emory, the representative of the Division, stated:

> "Thus, Harrison, through Magnuson, had a direct and constantly available source for the most

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5. Respondent's finding states in part:

> As to the latter, West Coast had in fact sustained a net loss of $203,063 for the nine months ended September 30, 1962, and had a cumulative deficit of $276,835 as of that date which had increased to $413,567 by the end of the year. In January 1963 West Coast sold for $770,000 its equipment leases for the four archery ranges opened in late 1962, which created a contingent liability by West Coast and Silver Buckle of about $851,000 for any rent defaults. At the time of that sale, one of the lessees was already in default on its rental payments. For the year ended February 28, 1963, during which it had sold the leases with respect to all five ranges then in existence, West Coast sustained a net loss of $59,376 and as of that date had a deficit of $167,477.

> current public and non-public information about all of the business affairs of Silver Buckle and West Coast at all times between May 1962 and April 30, 1964." (R. 4574).

The respondent also has disregarded the stipulation as its findings charge Harrison with a responsibility for West Coast's management decision and the operations of the lessees. Harrison did not know or have access to this information.

Price predictions made by Harrison and price predictions made by persons in other cases are not comparable. In *Alexander Reid & Co., Inc.* 40 SEC 986 (1962) the registrant's salesman predicted that the shares of Woodland Electronic Company, Inc. could double in a short period, triple in 90 days, go up three or four times, and climb to $15.00 or $20.00 within the year. Another salesman felt that it would rise like other low stocks that had reached a price of $40.00 and $50.00 a share. The representations made to members of the investing public in *Advanced Research Associates, Inc.,* Securities Act Release No. 4630 and Securities Exchange Act Release No. 7117 (1963) also referred to specific price figures and anticipated rises within a short period of time. These predictions were also made in a *brochure* distributed by the broker-dealer in conjunction with patently false statements of fact.

In *Underhill Securities Corporation,* Securities Exchange Act Release No. 7668 (1965) representations in the following form were held to be fraudulent:

> "That AMD 'should double in three months,' could 'double or triple (the customers's) money in a year or two,' and that AMD has prospects of 'becoming something like an IBM or a Polaroid.' "
> "Could 'practically guarantee' that the price of AMD stock would triple in four months . . . ."

Why isn't respondent concerned about the price predictions made by Walter Faubion, a registered representative of Walston & Co.? His prediction that Silver Buckle would hit $5.00 and go beyond that figure in another year assumed that West Coast's archery would be successful, and was much more flamboyant than Harrison's. (R. 954).

It is obvious that Harrison's trading activity was proper and that his casual statements to other broker-dealers were not part of a selling effort. They were made solely to other traders and were understood by the brokerage fraternity; to say that these remarks "contributed substantially" to the increase in trading and rise in price demonstrates that the respondent has been infected by the Division's refusal to understand the wholesale market.

3. Magnuson's sales of West Coast Stock during August-December, 1963.

Respondent refuses to believe that there was any tangible basis for optimism concerning the eventual financial success of West Coast during the first half of 1963. That this finding completely disregards substantial evidence in the Record is shown by the facts recited on pages 28 through 31 of this brief. There were

several significant efforts to obtain financial assistance during the last half of 1963 and, if any of the companies interested in West Coast at that time had honored moral commitments, West Coast easily would have achieved financial solvency. The respondent does not refer to the study made by the Brunswick Corporation. Since it ignores this very important undertaking, petitioners have placed additional material in the Appendix. (Appendix page 125-131). A letter from Glen Sherman, the president of West Coast (a person of whom the respondent is not critical) written to Magnuson on February 12, 1964 stated that the company was in better shape than when he first assumed the presidency in June. (Appendix page 88-93).

The shares of West Coast, following the merger in June, still sold like a mining security and financial information was not necessarily required to make an investment decision. Since the financial condition of the company was complex and prospects for additional financing quite good during this period, Magnuson did not have a duty under Rule 10b-5 to disclose any adverse financial information to purchasers of West Coast stock sold at this time, still assuming that he had this financial information. Although the sale of these shares constituted a technical violation of Section 5 of the Securities Act, it is respectfully submitted that the respondent has not established that Magnuson violated the anti-fraud provisions of the Act.

Harrison's confidence in West Coast's future is supported by the excess of purchases over sales of the

stock of West Coast by Pennaluna from June 11, 1963 to April 30, 1964. (R. 3717-3732). Common sense would indicate that Magnuson would not permit a corporation in which he owned 37½ percent of the stock to actively trade in the stock of another corporation which Magnuson knew to be in a failing financial condition. The duty of disclosure requires an evaluation of all information available at that time. The respondent's finding fails to recognize significant and favorable evidence.

The respondent's findings and reasoning lack clarity necessary to enable this Court to make a considered judgment without substituting its own findings. *Kahn v. S.E.C.,* 297 F.2d 112 (2nd Cir. 1961). It is respectfully submitted that this Court should reverse and set aside that portion of respondent's order relating to these issues.

THE DIVISION OF TRADING AND MARKETS CONDUCT OF THESE PROCEEDINGS WAS CONTRARY TO ADMINISTRATIVE DUE PROCESS OF LAW

These proceedings were commenced by an order for private proceedings on October 1, 1964. (R. 65-71). The Division felt that these proceedings were conducted privately because of an agreement by petitioners that a stipulated record would be prepared. Thomas W. Rae, Assistant Director of the Division at that time, further stated in a letter to petitioners' counsel on February 22, 1965 that "it was further anticipated that if a stipulation were agreed upon, the

respondents would submit an offer of settlement." A stipulation including only events occurring from May, 1963 forward was prepared and an offer of settlement discussed. Since settlement could not be accomplished, the full stipulation was completed. The stipulation only stated the manner in which various events transpired; it was not a stipulation of ultimate facts. Settlement discussions were held frequently and offers of settlement were extended to the Division, both formally and informally; on July 18, 1966, an offer to settle for a suspension of a period not to exceed 30 days was presented to Mr. Rae. Since he would not consent, the offer was not submitted to respondent. Mr. Rae, and representatives of the Division in the Seattle Regional Office, refused to state what suspension terms and days were acceptable to them and inferred to petitioners that all parties desired the respondent to set the number of days and suspension terms.

Petitioners waived a hearing examiner and proceeded directly to oral argument, without being advised that revocation and bar was being sought. Even assuming these proceedings are remedial, not penal, petitioners are entitled to know the severity of the allegations and the sanction to be expected if *conviction* should result.

On February 2, 1966, after the opening briefs of both parties were submitted, the Division deposed Anthony Vaghi under oath without notice to petitioners' counsel

or opportunity to appear. Mr. Vaghi appeared without counsel. Statements made at that deposition were highly prejudicial to petitioners. Vaghi testified that Harrison was his only source of information and that he did not do any research. (R. 4488). In fact, Gay had sent Vaghi brochures and information about the archery lanes. (R. 1592). Denial of the right to cross examine or rehabilitate a witness is a serious and unwarranted abuse of governmental power.

Petitioners further believe that representatives of the Division corresponded with the respondent concerning Harrison's performance while president of the Spokane Stock Exchange and that damaging comments were made in memorandums directed to the respondent, or made available to the respondent, without knowledge of the petitioners or opportunity to counter the comments. Lane Emory also argued facts beyond the scope of the stipulation and further breached his obligations as a representative of a government agency. Such activity violates the Administrative Procedure Act. (5 U.S.C.A. 554(d)). All of these matters were brought to the attention of respondent prior to filing this petition for review. The petition and motion for further rehearing was refused by respondent. (Supp. R. 4690-4699).

Petitioners are entitled to fair play by government agencies. The Division conduct violated basic concepts of administrative due process of law.

CONCLUSION

Petitioners obtained statements from persons active in the securities industry in the State of Washington for the purpose of establishing the character and reputation of Harrison and Magnuson. (Supp. R. 4671-4689). Although these statements were considered ex parte' communications by respondent, they should have been considered by respondent since character and reputation of the individuals involved is a fundamental factor in making a "public interest" determination. Respondent has not accepted these statements and has not properly evaluated the efforts made by Magnuson to obtain payment for West Coast's creditors and save the mining properties for the shareholders of Silver Buckle Mines, Inc. Magnuson has severed all relationship with Pennaluna and does not intend to engage in the securities business in the future. Pennaluna's books and records now conform to all requirements of the respondent; an examination made on March 24, 1966 revealed only minor and customary reporting problems.

The technical violations occurring during late 1963 and the record-keeping violations found by the respondent cannot support a grave sanction of revocation and bar. The "whole record" does not support respondent's finding of violations of the anti-fraud provisions of the Acts and Section 5 of the Securities Act prior to May, 1963. The order issued by the respondent must be reversed and set aside and this case re-

manded to the respondent for a further determination consistent with the record and respondent's administrative obligations.

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I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

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